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C O N F I D E N T I A L SECTION 01 OF 03 KINSHASA 001067

SIPDIS

DEPT PASS TO USTR

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TAGS: ETRD ECON EFIN EINV CG
SUBJECT: SIGNIFICANT TRADE BARRIERS REMAIN IN EASTERN CONGO

Classified By: W. BRAFMAN FOR REASONS 1.4 b/d.

Summary

¶1. (SBU) Summary. Eastern Congo continues to face significant trade growth barriers. Infrastructure, security, access to credit, taxation, foreign competition, bureaucratic obstacles, insufficient information and internal politics are all serious obstacles that discourage and even reverse growth efforts, particularly in the manufacturing sector. South Kivu alone has reportedly lost at least 18,000 jobs since ¶1996. The GDRC devotes only limited attention to removal of these barriers. End Summary.

Road to Nowhere, Lights Out

¶2. (U) Inadequate infrastructure is the primary factor that hamstrings trade growth in many eastern Congo regions, particularly the Kasai and Kivu provinces. Severely deteriorated or non-existent roads and insufficient and unreliable power supply hamper cost-effective production and distribution. For example, Sotexki, a Congolese-owned and operated textile plant located in Kisangani, Kasai Orientale, functions at an estimated ten percent of its capacity in part because of problems at the Societe National d'Electricite (SNEL). SNEL is planning to increase capacity in Kisangani from 6 to 11 Megawatts, but the provincial director of the FEC (Federation des Enterprises du Congo, a chamber of commerce) advises that this still will not meet demand.

Inadequate Security and Credit

¶3. (SBU) Security problems are the greatest growth impediment in North and South Kivu. Business persons in both provinces repeatedly said that the economic sector can absolutely not advance without security. Violence and fear of violence have particularly decimated the agricultural sector; in some cases entire villages have been displaced. Farmers are frequently afraid to return to their fields and, once they do, roving militias and poorly paid Congolese military seize crops and livestock to sell and consume.

¶4. (C) Business owners throughout the eastern Congo, particularly among small- and medium-sized enterprises, state that they have little access to credit. The Commercial Bank of the Congo (BCDC) in Kisangani and the Kivus makes very few loans. The BCDC in Lubumbashi reported that it has a loan portfolio of several million dollars, and one client with a credit line of USD one million, although most borrowers are foreign-owned interests. Companies that seek multi-million dollar loans must normally obtain them outside the DRC. The BCDC's policies exclude loans to small and start-up businesses, because a borrower must have at least USD 5,000 on deposit and provide collateral. (Comment: It is unclear if business owners are unable or just unwilling to obtain loans from banks. Many Congolese avoid the banking system not only because they lack faith in bank deposit security, but also to avoid disclosing assets and therefore triggering tax liability on otherwise undeclared cash. End Comment.)

¶5. (U) Credit cooperatives and micro-finance institutions have begun to fill the credit void in the provincial capitals, although it is not clear if they have sufficient assets to foster widespread economic growth. There are at least two such groups in Kisangani, Credit Boyomais and a USAID-sponsored program through Hope International, although Credit Boyomais' rates are high (8 percent per month) and are limited to borrowers that the cooperatives' owner knows personally. Credit cooperatives and micro-finance operations offer lower rates in Goma and Bukavu than the BCDC, but again availability is likely limited to the few who live in the towns and hear of the institutions.

The Taxman Cometh

¶6. (C) Onerous, arbitrary taxes and bureaucratic red tape also penalize and deter growth. The administrative time expended in determining, negotiating, paying and even avoiding taxes may create a burden equal to or greater than the tax liability itself. Most eastern Congolese business

owners were unable even to estimate their tax bill, although some offered a figure of thirty to forty percent of revenue. Even the North Kivu Governor could not explain his province's tax structure. National, provincial and local governments each impose a variety of taxes and other governmental requirements, although not all are legal. A South Kivu factory manager reported that various government officials impose as many as forty different taxes on his company and that his accountant spends as much as eighty percent of his time determining and negotiating tax liability. Several officials per day may visit a business, often trying to collect the same tax. Many business persons, particularly in South Kivu, reported that local officials often create fictitious taxes.

¶7. (C) Export taxes in particular impose an obvious obstacle to trade growth. Factory managers and traders report that the DRC's export taxes of up to four percent creates a strong export disincentive. South Kivu alone has reportedly lost at least 18,000 jobs since 1996 due in large part to the decline of export markets. Business owners in the Kivus reported that Rwanda imposes only a one percent export tax, and that other neighboring countries' export liabilities are similarly low, discouraging the establishment of legal export businesses in the DRC. In the Kivus, merchants often illegally export goods themselves or trade with Rwandans who enter the DRC and do the smuggling. Katangan businesses also report substantial illegal exports into Zambia, particularly in the mineral sector.

¶8. (SBU) Provincial governments appear to be taking some measures to reduce tax liability and streamline collection. The South Kivu Vice Governor for Finance and Economy reported that he has created an internal tax audit division to eliminate double and illegal taxation. Both the Province Orientale Vice Governor for Finance and Economy and the North Kivu Vice Governor reported cooperation with the GDRC in Kinshasa that resulted in the elimination of all or most double taxation. OFIDA (the Congolese customs agency) established one-stop customs windows ("guichet unique"), although so far it does not seem to have substantially reduced customs fraud.

Competition is Tough

¶9. (U) Outside the DRC, lower tax burdens and production and transport costs create powerful external competition. As mentioned above, countries that border the DRC have lower export duties that attract business. Many of these countries also have more developed infrastructure, including rail and road systems, that enable cheaper, faster goods transport. The GOR provides some support to Rwandan exporters, primarily in the agricultural sector. Lower-cost Asian-manufactured goods are clearly harming the Congolese manufacturing industry, particularly in the textile sector. Many DRC markets sell Chinese-made fabrics for half the price of identical, higher-quality Congolese textiles. (Comment: Many Congolese business managers seem to lack updated information and knowledge of modern business management techniques. For example, several asked for information about AGOA. One factory manager noted surprisingly that he no longer had a captive market and had to pursue customers. End Comment.)

Political Affilation Matters

¶10. (C) Finally, several business people throughout eastern Congo said that political party affiliation can still substantially affect the ease of doing business. For example, the textile factory manager in Kisangani claimed that, because the factory owner belongs to one political faction, other political factions avoid doing business with the factory. Business owners in the Kivus, including a North Kivu FEC representative, said that the government creates a business climate that is much more hostile to them than in provinces that President Kabila's faction dominates, such as Katanga. For example, several North Kivu businessmen said that ministries will not give North Kivu businesses permission to operate outside of their province and will not honor agreements made under prior governments. However, the North Kivu Vice Governor for Finance and Economy vehemently denied this assertion and said that these businessmen merely resent that they can no longer conduct business free of government restriction.

Comment

¶11. (C) The GDRC and the provincial governors seem only to be beginning to understand the importance of enacting reforms that support the trade sector. Parliament did recently pass a new Customs Code that emphasizes fraud and red tape reduction. Further, as discussed above, some officials recognize the importance of tax reform, even if they are not able to implement it. However, given their status as

appointed officials, most are probably unwilling and even unable to push the central government too hard. In particular, in Province Orientale, the government seemed ill-informed and ill-prepared to support economic development. Nevertheless, some promising signs emerged in South Kivu, where the forward-thinking young Vice Governor has now engaged the FEC in monthly meetings to discuss economic issues. End Comment.
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